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SENSITIVE

STATE FOR E, P, EUR/SE AND EB  
TREASURY FOR U/S TAYLOR AND OASIA - MILLS  
NSC FOR QUANRUD AND BRYZA

E.O. 12958: N/A

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SUBJECT: TURKEY'S ECONOMY APRIL 25: POSITIVE NEWS ON  
TREASURY APPOINTMENT; CENTRAL BANK CUTS SHORT-TERM RATES

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1. (SBU) Summary: Some positive news came at the end of a relatively quiet week in Turkish markets: the GOT announced a well-regarded macro-economist bureaucrat, Ibrahim Canakci, to replace Faik Oztrak at Treasury. The Central Bank announced a 3 percentage point cut in its short-term borrowing rate, which led immediately to a one percentage point decline in T-bill yields. Market sentiment at end April is much improved from earlier in the month, but investors both local and foreign remain wary of AK's commitment to the reform program. Further improvements on interest rates (below the low 50's) are likely only to follow tangible progress on reforms, as measured by the next IMF staff mission, now scheduled to start May 21. End Summary.

Markets Quiet, T-Bill Rates Decline  
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2. (U) On April 25, yields on the lira T-bills declined about one percentage point to 55 percent compounded, immediately following the Central Bank's announcement of a rate cut (see below). T-bill yields, trading all week at the 56-57 percent level, are now expected to decline to the low 50's. The lira was flat, trading at TL 1,595,000 to the dollar while the Istanbul Stock Exchange 100 index was up 1.3 percent.

Central Bank Cuts Key  
Lira Borrowing Rate  
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3. (SBU) At OOB April 25, the Central Bank announced a cut in its short-term borrowing rates: the key lira borrowing rate, one week maturity, went from 44 to 41 percent simple (or to about 51.5 percent compounded).

4. (SBU) Comment: The markets exerted some pressure for this rate cut and responded immediately by lowering T-bill yields. PM Erdogan also predicted interest rates declines in his weekly meeting with AK parliamentarians April 24. In an April 24 meeting with Central Bank Governor Serdengeçti on other topics (Iraqi assets), the Governor told us such political pressure didn't work on him - former MinState Derviş's many attempts to dictate interest rate policy had just slowed down the Central Bank decision making process. However, he continued, the outlook on inflation was turning positive. Serdengeçti spoke about the need for an inflation-targeting Central Bank to help shape expectations through interest rate policy, not just react to market perceptions. Today's decision may be viewed by some analysts as premature (given continuing strong concerns in the market), but it may also help bring down inflationary expectations. End Comment.

New Treasury Undersecretary A Good Choice  
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5. (U) On April 26, MinState Ali Babacan announced the appointment of Ibrahim Canakci as Treasury Undersecretary, replacing Faik Oztrak. (Note: "Undersecretary" in case of Treasury and some other GOT agencies is the head of the agency.) Canakci, 41 years old, worked at the State Planning Organization from 1986-2000, rising to head of the Economic Forecasting Department. While at SPO, he earned a Masters in

Economics from Michigan State University. In 2000, he moved to the Bank Regulatory and Supervision Agency, first to run the research department, later to be the Deputy Chairman. he is married, with two children and speaks fluent English.

16. (SBU) Comment: The Treasury Undersecretary runs the GOT's main economic policy agency and serves as the day-to-day contact with the IMF and World Bank. Canakci, well known to the Embassy since his SPO days, is an excellent choice; markets are likely to be relieved given the other, less credible names bandied about. He has a strong macro-economic background (and worked for Faik Oztrak when they both were at SPO), understands and supports the reform program, and furthermore has a good background on banking sector issues. Canakci is religiously observant (observes the dawn-dusk Ramadan fast), though he is not an AK partisan and has independent views on the party's economic policies. His low-key, mild-mannered approach may well help in educating AK politicians on economic reforms in a non-confrontational way.  
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